2/2/81
B 5350-2 U

The Manufacturers Hanover
Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, FEBRUARY 2, 1981 VOLUME XVIII, NUMBER 5

No Quick Cure From Decontrol

As promised during the election campaign, President Reagan lifted all controls on crude oil prices and allocations last week. These had been in effect since the Nixon Administration's general wage-price freeze imposed in August, 1971. This action will undoubtedly boost prices at retail--but these increases would have occurred anyway, albeit more gradually. Full decontrol was scheduled to occur by October 1. The impact of President Reagan's action is expected to be slight in the near term. Even before total decontrol, nearly three-quarters of all domestically produced crude was free to be priced at market levels. Thus, the amount of oil subject to an immediate price rise is not all that large.

What is more, sizable stocks in our nation's refineries will further cushion the price impact of decontrol. For example, there are now 52 days' supply of distillate fuel oil, which includes home heating oil, and about 40 days' supply of motor gasoline. Consequently, with inventories bulging and consumer conservation efforts expected to intensify, the oil producers may be reluctant to pass quickly on to the public the full price effects of oil decontrol. In addition, if weather patterns return to normal in the Northeast—to date the number of degree days is running 34 per cent above comparable year-ago levels—then demand for residential heating oil will soften, preventing producers from lifting prices significantly above present quotes.

Although the acceleration of decontrol will boost oil company revenues (and government tax revenues in the form of both income and windfall profits taxes), no immediate increase in supplies of domestic crude oil or additional drilling above that already scheduled should be expected. The oil producers stepped-up sharply their search for new oil in many areas last year, after the decontrol program started. As a result, drilling activity is already at record-high levels, increasing by more than 56 per cent in 1980. But despite the enhanced exploration activity, domestic oil production in 1980 still stood 6½ per cent below 1973 production levels.

Hence, last week's move by President Reagan may be viewed initially more as a symbolic first step toward easing government regulation of business. It will allow the market mechanism to allocate gasoline, home heating fuel and other refined products, rather than government fiat. While no significant alteration of supplies is expected in the near future, recent history indicates that higher prices will eventually induce more conservation by consumers both as motorists and as homeowners.

Inflation Lingers On

As noted above, this program will add somewhat to our already high inflation rate. Exactly by how much is uncertain, since it depends on how quickly and by how much oil companies raise prices. Estimates vary but an addition of 0.3 to 0.5 per cent in 1981 is not unreasonable. Meanwhile, inflation continued its double-digit rate of rise in 1980, averaging 13.4 per cent, compared with 11.3 per cent the year before. In December, prices of energy products were one of the major contributors to the 1.1 per cent climb in the consumer price index—the largest jump since the 1.4 per cent increase registered last March. Energy prices surged by 1.5 per cent in December, paced by a 3.4 per cent increase in the cost of home heating oil. Housing costs continued their upward spiral which began in October as a result of rising interest rates. Financing costs jumped by 4.1 per cent, reflecting the sharp rise in mortgage rates while home purchase prices remained the same.

The cost of food went up sharply both at the supermarket counter and when eating out. Prices of grocery store foods rose by 1.1 per cent, propelled by soaring prices of pork, poultry, fish and eggs, more than offsetting the decline in beef prices which dropped by 0.9 per cent. Similarly, prices of vegetables, cereals, bakery items, fresh milk, sugar, artificial sweeteners and peanut butter posted substantial increases. The index for restaurant meals advanced by one per cent.

Balancing The Federal Budget . . .

One of the more persistent problems that the new Administration has focused on is the dismal state of Federal government finances. Clearly, such attention is not misplaced. In recent months, the budget outlook has worsened substantially due to a wide

Copyright 1981
Manufacturers Hanover Trust Company
350 Park Avenue, New York, NY 10022

variety of factors. These range from the continued swelling of transfer payments due to inflation, the increasing likelihood of another dip in economic activity and the financial burden of servicing an ever-expanding Federal debt at prevailing high interest rates. What is more, chances of cutting taxes and stepping up defense spending are becoming increasingly likely, clouding even further the prospects for an early balancing of the Federal budget.

Indicative of the magnitude of the problem was the December budget outcome. Expenditures exceeded revenues by $7.3 billion—almost five times the size of the December, 1979 deficit. This brought the fiscal year-to-date red ink total to a whopping $33.6 billion, more than $9 billion higher than the comparable period in fiscal 1980. If these trends persist, the budget deficit for the fiscal year as a whole could reach almost $80 billion—the largest fiscal year deficit ever posted. In this event, Federal government borrowing requirements could well exceed $100 billion, including the financial requirements of the off-budget agencies.

. . . Remains An Elusive Goal

The big question, of course, is: Will these trends persist? Ominously, the answer appears to be "yes." For it now seems that the gap between spending and revenues may widen in the coming months. The

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 1/21/81	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	128.706	– .576	+ 2.530
Loans to Depository Inst.	1.419	+ .087	+ .216
Float	3.880	– .609	– 1.386
Total Reserve Bank Credit	143.232	– .459	+ 5.169
Treasury Deposits with Federal Reserve Banks	3.109	+ .024	+ .036
Currency Outside Banks	118.043	– 1.468	+ 8.466
Member Bank Reserves:			
Required	42.180	+ .940	– 2.965
Excess (Deficiency)	.737	– .004	+ .611
Total Reserves Held	42.917	+ .936	– 2.354
Net Borrowed Reserves	.559	+ .073	– .441
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	92.520	– .463	+12.328

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M-1A	370.8	+ 8.8‡	+ 1.8‡
M-1B	416.2	+ 4.1‡	+ 7.0‡
M-2 (December '80)	1,674.8	+ 7.6	+ 9.8
L (October '80)	2,323.5	+ 11.8	+ 9.0

†Seasonally adjusted. * Seasonally adjusted annual rate. ‡Four-week moving average.

New York Money Market

Offering Rates 1/30/81	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	14.78%	13.85%	12.64%
* Federal Agencies	15.36	15.65	14.50
* Project Notes—Taxfree (46% Taxable Equivalent)	12.04	12.50	13.43
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
*Secondary Market—Prime	16.50	15.25	

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	16.00%	Mar.	16.40%
15- 29 days	16.13	Apr.	15.90
30- 59 days	16.25	May	15.75
60- 89 days	16.00	Jun.	15.40
90-179 days	14.00	Jul.	14.90
180-270 days	13.00	Aug.	14.75

‡Industrial Paper—Prime		†Federal Funds	
30- 89 days	16.38%	Effective Rate	17.20%
90-120 days	16.00		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	4th Q'80	$ 2,741	$ 2,637	$ 2,496
Gross National Product (1972 Dollars)*	4th Q'80	$ 1,490	$ 1,472	$ 1,491
Percent Change, Annual Rate	4th Q'80	5.0%	2.4%	0.6%
Change in Consumer Prices (all urban consumers)*	Dec '80	13.2%	12.0%	14.4%
Change in Producer Prices*	Dec '80	7.2%	7.2%	9.6%
Civilian Employment (Thousands of Persons)†	Dec '80	97,282	97,339	97,781
Unemployment as % of Civilian Labor Force†	Dec '80	7.4%	7.5%	6.0%
Personal Income*	Dec '80	$ 2,282	$ 2,260	$ 2,028
Leading Indicators Composite Index (1967=100)†	Dec '80n	136.6	137.7	135.2
Industrial Production Index (1967=100)†	Dec '80	150.7	149.2	152.5
Net Change in Consumer Installment Credit†	Nov '80	$ 0.84	$ 0.70	$ 2.69
U.S. Merchandise Trade Balance†	Nov '80	–$ 0.79	–$ 0.97	–$ 1.62
Plant and Equipment Expenditures*	1st Q'81	$310.59(a)	$297.30(a)	$291.89
Private Housing Starts (Thousands of Units)*	Dec '80	1,548	1,563	1,548
New Construction Expenditures*	Nov '80	$ 231.8	$ 226.2	$ 239.4
Total Business Inventories†	Nov '80	$ 458.2	$ 456.5	$ 426.0
Total Business Sales†	Nov '80	$ 329.1	$ 325.8	$ 298.9

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. a-Anticipated.

economy could experience a more pronounced weakening than expected. Defense spending may well be increased sharply above present levels. Additionally, despite the added emphasis being placed on national defense, the largest proportion of the spending increases posted during the first quarter of fiscal year 1981—almost one half of the $22 billion year-over-year gain—was accounted for by stepped-up income security outlays, of which inflation-indexed Social Security payments are a major component. By contrast, increased defense outlays accounted for only about one quarter of the spending gain.

Thus, with income security outlays already rising rapidly, additional countercyclical spending associated with the weakening economy, such as extended unemployment insurance benefits, and higher defense spending would push expenditure totals even higher than the $670 billion now estimated. And if, on top of this, an across-the-board personal income tax cut is implemented (and revenues shrink accordingly, a development that the immediate decontrol of domestic oil prices will not offset), the budget outlook becomes almost too dismal to contemplate. This would have profound implications both for the financial markets and for the ability of the new Administration to balance the Federal budget—even within the next four years. ■

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Negotiable Time CD's Weekly Reporting Banks			
Nationwide (1/14/81)	114,256	– 527	+21,936
New York City (1/14/81)	28,877	– 277	+ 8,826
Commercial Paper (1/14/81)	128,569	+ 2,646	+13,095

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/14/81)	173,118	– 111	+14,430
New York City (1/14/81)	51,558	+ 315	+ 4,293

Total Loans Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/14/81)	429,197	– 3,183	+29,767
New York City (1/14/81)	102,194	– 1,145	+11,759

Financial Markets

	Friday 1/30/81	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	14.55%	– 1.99	+ 1.90
180-Day Bills†	13.58	– 2.42	+ .73
Longest Bills†	12.48	– 2.27	+ .04
Recent Issues:			
15½s 12/31/82	13.70	– .02	
14s 12/31/84	13.09	– .12	
13s 11/15/90	12.60	– .47	
12¾s 11/15/10	12.23	– .15	
Municipals:			
Bond Buyer–20 Bond Index* (1/29/81)	9.91%	+ .23	+ 2.39
Blue List Total ($ Million)	$ 630	– $ 19	– $ 236
30-Day Visible Supply ($ Million)	$1,696	– $ 47	+ $ 620
Total	$2,326	– $ 66	+ $ 384
Corporates:			
Moody's Aa Composite (1/29/81)	13.64%	– .01	+ 1.77
Money Mgr.–30-Day Supply ($ Million)	$3,713	– $758	+ $1,973
Stocks:			
Dow-Jones Averages:			
Industrials	947.27	+ 7.08	+ 65.79
Transportation	402.16	+ 10.55	+ 118.66
Utilities	112.82	+ 1.06	+ 2.50
65 Stocks	370.36	+ 5.09	+ 51.51
Standard and Poor's 500 Stocks	129.55	– .68	+ 14.43
N.Y.S.E. Composite Index	74.27	– .45	+ 8.00
N.Y.S.E. Avg. Daily Vol. for Week (000's)	38,822	– 142	– 15,790

* 46% Taxable equivalent 18.35%.

† Bond equivalent.

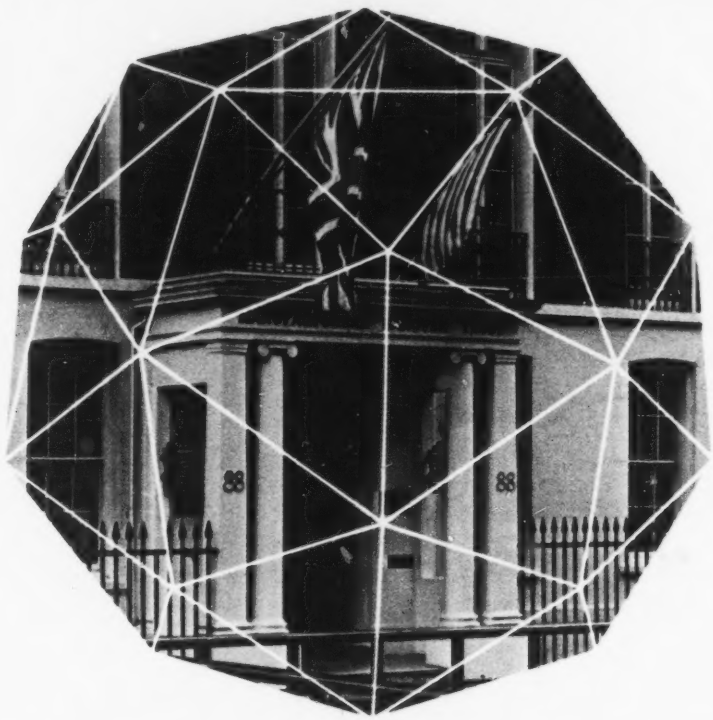
International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 1/30/81	Week Ago
Overnight	17.50%	19.25%
1 month	17.63	19.25
3 month	17.38	18.88
6 month	16.63	17.25
1 year	15.63	16.13
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	12.95%	13.05%
Long Term (7 to 15 yrs.)	12.85	12.95

FOREIGN EXCHANGE SPOT RATES

New York Opening (1/30/81)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02948	33.92
Canada	.8360	1.1962
Denmark	.1537	6.5050
France	.2050	4.8780
Germany	.4721	2.1180
Italy	.0009980	1002.00
Japan	.004857	205.90
Mexico	.04272	23.41
Netherlands	.4354	2.2970
Switzerland	.5187	1.9280
U.K.	2.3820	.4198

The Geobankers can put money to work for you in any convertible currency.



GEOBANKING®.

It is the way of worldwide banking at Manufacturers Hanover, a major U.S. bank with nearly $50 billion in assets and a tradition of service dating back more than a century.

GEOBANKING DEPOSIT FACILITIES.

Nearly $40 billion in local and international currency deposits are currently entrusted to the Geobankers on a global basis. By governments, banks, businesses and individuals.

These deposits take the form of current accounts to concentrate funds for business payments. Certificates of deposit that offer excellent marketability. Time deposits for longer-term investment. And a variety of other deposit accounts for earnings plus liquidity.

Put the total global commitment of Manufacturers Hanover to work for you. Contact a Geobanker today.

MANUFACTURERS HANOVER

The banking source. Worldwide.

Headquarters: 350 Park Avenue, New York, N.Y.

Member FDIC